THE FOUR-PART TEST

1. Technological in Nature (§41)
The activity performed must fundamentally rely on principles of:

- Physical Science;
- Biological Science;
- Engineering; or
- Computer Science

2. Permitted Purpose (§41)
The activity must relate to a new/improved business component’s:

- Function;
- Performance;
- Reliability; or
- Quality

3. Elimination of Uncertainty (§174)
The activity must be intended to discover information to eliminate uncertainty concerning the capability, method or design for developing or improving a product or process.

4. Process of Experimentation (§41)
The taxpayer must engage in an evaluative process designed to identify and evaluate more than one alternative to achieve a result

For example: modeling, simulation or a systematic trial and error methodology.
INTERNAL USE SOFTWARE: THE SEVEN-PART TEST

WHAT QUALIFIES AS RESEARCH & DEVELOPMENT?

Innovative (§1.41 - 4)
The software is intended to result in:

- Reduction of Cost;
- Improvement in Speed; or
- Other improvement(s) that is(are) both substantial

This is a measurable objective standard not a determination of the unique or novel nature of the software or the software development process.

Significant Economic Risk (§1.41 - 4)
Taxpayer commits substantial resources to the development and there is substantial uncertainty because of technical risk that such resources would be recovered within a reasonable period.

Not Commercially Available (§1.4 - 4)
The software cannot be purchased, leased, or licensed and used for the intended purpose without modifications that would satisfy the Innovative and Significant Economic Risk requirements.

ABOUT KBKG

KBKG is a nationwide firm specializing in R&D Tax Credits, Cost Segregation, Green Building Incentives, and more. Our engineers and tax experts have performed thousands of tax projects that saved our clients hundreds of millions of dollars in benefits since 1999.

As leading educators in our field, we have been invited to speak to thousands of CPAs and tax professionals by the most prominent associations in the industry. Our goal is to bring value to our clients by providing quality service, building long-term relationships, and ensuring a high standard of professional ethics.